APPENDIX

SEPTEMBER TERM — October 22, 1985

Before Honorable James E. Barrett, Honorable John P. Moore and Honorable William H. Timbers*, Circuit Judges

FEDERAL DEPOSIT INSURANCE CORPORATION and DEPOSIT INSURANCE NATIONAL BANK OF OKLAHOMA CITY, OKLAHOMA,		
	Plaintiffs-Appellants.	No. 84-2350
vs.		
PAULINE McKNIGHT, PAULINE OIL AND GAS COMPANY and ROCKET OIL COMPANY,		
	Defendant-Appellees.	

Upon the motion of the appellee, Rocket Oil Company, the Court's order of October 10, 1985, setting bond for the purpose of stay pending certiorari is amended to provide that the amount of the bond applicable to Rocket Oil Company shall be $1,400,000.00.

(s) *Howard K. Phillips*
HOWARD K. PHILLIPS, Clerk

*Of the Second Circuit, sitting by designation

[APPENDIX]

SEPTEMBER TERM — October 10, 1985

Before Honorable James E. Barrett, Honorable John P. Moore and Honorable William H. Timbers*, Circuit Judges

FEDERAL DEPOSIT INSURANCE CORPORATION and DEPOSIT INSURANCE NATIONAL BANK OF OKLAHOMA CITY, OKLAHOMA, Plaintiffs-Appellants,	)	No. 84-2350
v.	)	
PAULINE McKNIGHT, PAULINE OIL AND GAS COMPANY and ROCKET OIL COMPANY, Defendants-Appellees.	)	

This matter comes on for consideration of appellees' motions to stay issuance of mandate in the captioned case pending filing of a petition for writ of certiorari, and appellant's response thereto.

Upon consideration whereof, the mandate is stayed until October 21, 1985, pending notification that the appellees have caused to be filed with the United States District Court for the Western District of Oklahoma a surety bond in the amount of One Million Seven Hundred Fifty Thousand Dollars ($1,750,000), securing payment of the judgments directed by this Court to be entered in the captioned case. If the required bond is timely filed, the stay of mandate will be continued pending certiorari.

HOWARD K. PHILLIPS, Clerk

by *Robert L. Hoecker*
Chief Deputy Clerk

*Of the Second Circuit, sitting by designation

JULY TERM — September 17, 1985

Before Honorable James E. Barrett, Honorable Monroe G. McKay, Honorable James K. Logan, Honorable John P. Moore, and Honorable William H. Timbers*, Circuit Judges

FEDERAL DEPOSIT INSURANCE COMPANY, etc., et al, Plaintiffs-Appellants,	)	
vs.	)	No. 84-2350
PAULINE McKNIGHT, PAULINE OIL AND GAS COMPANY and ROCKET OIL COMPANY, Defendants-Appellees.	)	

This matter comes on for consideration of the petitions for rehearing and suggestions for rehearing en banc filed by appellees in the captioned cause.

Upon consideration whereof, the petitions for rehearing are denied by the panel that rendered the decision sought to be reheard.

The petition for rehearing having been denied by the panel to whom the case was argued and submitted, and no member of the panel nor judge in regular active service on the Court having requested that the Court be polled on rehearing en banc, Rule 35, Federal Rules of Appellate Procedure, the suggestion for rehearing en banc is denied.

Chief Judge William J. Holloway, Jr., and Judge Stephanie K. Seymour did not participate.

(s) *Howard K. Phillips*
HOWARD K. PHILLIPS, Clerk

[APPENDIX]

PUBLISH

[Filed August 2, 1985]

UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

FEDERAL DEPOSIT INSURANCE CORPORATION and DEPOSIT INSURANCE NATIONAL BANK OF OKLAHOMA CITY, OKLAHOMA, Plaintiffs-Appellants,	)	No. 84-2350
vs.	)	
PAULINE McKNIGHT, PAULINE OIL AND GAS COMPANY and ROCKET OIL COMPANY, Defendants-Appellees.	)	
FEDERAL DEPOSIT INSURANCE CORPORATION and DEPOSIT INSURANCE NATIONAL BANK OF OKLAHOMA CITY, OKLAHOMA, Plaintiffs-Appellants,	)	No. 84-2352
vs.	)	
ALL SOULS EPISCOPAL CHURCH, Defendant-Appellee.	)	

Appeal from the United States District Court
for the Western District of Oklahoma
(D.C. Nos. CIV-83-185-W, CIV-83-186-W,
CIV-83-188-W, and CIV-83-1794-W)

Charles V. Wheeler and Sidney G. Dunagan of Gable & Gotwals, Tulsa, Oklahoma, for Plaintiffs-Appellants.

B. J. Rothbaum, Jr., of Linn & Helms, Oklahoma City, Oklahoma, for Defendant-Appellee Rocket Oil Company.

Michael Paul Kirschner of Hastie and Kirschner, Oklahoma City, Oklahoma, for Defendant-Appellee All Souls Episcopal Church.

George W. Dahnke and Merrilyn L. Blackburn of Hastie and Kirschner, Oklahoma City, Oklahoma, on the brief for Defendants-Appellees Pauline McKnight and Pauline Oil and Gas Company.

Before BARRETT, MOORE and TIMBERS,* Circuit Judges

MOORE, Circuit Judge

This is an appeal from a judgment denying plaintiffs, Federal Deposit Insurance Corporation (FDIC) and Deposit Insurance National Bank of Oklahoma City (DINB), relief on their claim for restitution of money mistakenly paid on cashier's checks issued by the insolvent Penn Square Bank, N.A. (Penn Square). The district court concluded that even though the plaintiffs established a *prima facie* case for restitution, their recovery was barred by the final payment rule of the Uniform Commercial Code (U.C.C.). We conclude the trial court correctly decided the question of restitution, but in applying the U.C.C. to this case, it overlooked the consequences of Penn Square's insolvency. Since those consequences placed the defendants in the position of creditors of an insolvent national bank, and since the federal law providing for liquidation of a national bank must take precedence over the U.C.C., we reverse.

This action has its genesis in a number of separate transactions negotiated by the defendants immediately prior to the closing of Penn Square. While the district court found there was no evidence that any defendant knew of Penn Square's impending failure when these transactions

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*Honorable William H. Timbers, United States Circuit Judge for the Second Circuit, sitting by designation.

occurred, the proximity of the events to Penn Square's insolvency is the underlying cause of what followed. On July 1, 1982, two banking days prior to Penn Square's closing, defendant Rocket Oil Company redeemed a certificate of deposit (CD) in the face amount of $1.5 million for $1,480,273.98, taking a Penn Square cashier's check of even amount in place of cash. On the following day, defendants Pauline Oil Company and Pauline McKnight liquidated both matured and unmatured CD's and converted the proceeds to cashier's checks totaling $323,538.46. On the same day, defendant All Souls Episcopal Church redeemed two CD's and other paper and exchanged the proceeds for three cashier's checks in the aggregate of $452,527.25. All of the checks received by defendants were deposited in their own banks for collection.

At 7:00 p.m., Monday, July 5, 1982, before any of the checks were presented for payment, the Comptroller of the Currency of the United States declared Penn Square insolvent under 12 U.S.C. § 191, and appointed FDIC to act as receiver pursuant to 12 U.S.C. § 1821(c). FDIC, in turn, organized DINB as a new bank through which insured parties were to be paid. FDIC transferred to DINB funds with which to accomplish this purpose and to conduct operations.

One of the first tasks performed by FDIC employees was the programming of the bank's computer to reject any items in excess of $100,000 drawn against Penn Square accounts. This was done to avoid payment of any withdrawal in excess of the deposit insurance limits. By oversight, the program was not extended to cover cashier's checks issued by Penn Square. Before this error was discovered on July 7, all of the cashier's checks issued to defendants had been presented by the collecting bank and paid by plaintiffs. Upon discovery of these payments, this action was commenced to recover the difference between the insured amounts and the amounts actually paid.

As the facts were not in dispute, the issues were ultimately resolved on cross-motions for summary judgment. FDIC asserted that upon the date of insolvency, all outstanding and unpaid cashier's checks of Penn Square had been converted to deposits by operation of law.[1] This contention was based upon 12 U.S.C. § 1813(1)(4), which states: "The term 'deposit' means . . . [an] outstanding . . . cashier's check, . . . issued in the usual course of business *for any purpose* . . . ." (Emphasis added.) FDIC further contended that payment of any of the cashier's checks in excess of $100,000, the insured amount of any deposit, was a mistake subject to restitution.

Defendants countered with many contentions, principally that they accepted the Penn Square cashier's checks in good faith and that they were thus holders in due course. Accordingly, they argued they were entitled to application of the "final payment rule," which states that payment of any instrument is final as to a holder in due course. U.C.C. § 3-418; Okla. Stat. tit. 12A, § 3-418 (1971).

After consideration of the arguments, the trial court concluded the plaintiffs made a *prima facie* case for restitution. The court, in effect, reasoned that 12 U.S.C. § 1813 (1)(4) governed, that defendants were only entitled to payment of the insured amount, and that payment of sums of money greater than the insured amount constituted unjust enrichment. We concur with this reasoning. Yet, the court went on to conclude that since plaintiffs' claims to restitution were based on negotiable instruments, "special rules" in defense were applicable. The court then proceeded to apply the final payment rule. Holding payment of the cashier's checks constituted final payment, the court barred recovery of restitution. We disagree.

Application of the final payment rule was erroneous for a number of reasons. First, as the trial court recog-

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[1] Some defendants contend this issue is raised for the first time on appeal. Clearly, that is not the case.

nized in concluding plaintiffs had made a *prima facie* case, the consequence of insolvency and the resultant application of the apposite portion of the Federal Deposit Insurance Act [12 U.S.C. § 1813(1)(4)] converted the cashier's checks from negotiable instruments to deposits by operation of law. Thus, the "special rules" applicable to negotiable instruments are irrelevant.

Second, and of greater importance, when the uncollected cashier's checks were finally presented, the defendants were creditors of an insolvent national bank. As such, their rights and liabilities became fixed by the National Bank Act. When that act provides a remedy, it takes precedence over state law. *Cf. Harmsen* v. *Smith*, 693 F.2d 932 (9th Cir. 1982), *cert. denied*, 104 S. Ct. 89 (1983). Here, the National Bank Act provides for the liquidation of the debts of an insolvent national bank. Accordingly, payment of the debts of Penn Square following insolvency had to have been made in compliance with the National Bank Act, not the Uniform Commercial Code.

Finally, neither the good faith of the defendants nor the source of the funds used to acquire the cashier's checks is of consequence. Despite their good faith and the origin of the funds,[2] the defendants have been cast by law into

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[2] Some defendants have argued because the money used to acquire the cashier's checks came from their deposits, the cashier's checks represented "their" money.

[3] Despite the effort made by some defendants to otherwise cast ther role, this conclusion is inescapable. Even had insolvency not occurred, as holders of unpaid cashier's checks drawn on Penn Square, defendants were still creditors. We have previously made plain a cashier's check is nothing more than a debt of the bank accepted by it upon issuance. *Anderson, Clayton & Co.* v. *Farmers National Bank of Cordell*, 624 F.2d 105 (10th Cir. 1980). Moreover, even though defendants' banks had "paid" the checks, payment did not come from the issuing bank, Penn Square. Hence, the "payment" received by defendants was not final, and the checks were simply in the process of collection when the Penn Square insolvency occurred. *Cf.* U.C.C. § 3-501.

the role of creditors,[3] and, as such, they must be treated in a circumscribed fashion.

The seminal point is the closing of Penn Square. That event not only triggered the liquidation process, but it also cast in stone the relationship of defendants to the bank. "It is well settled that the rights and liabilities of a bank and the bank's debtors and creditors are fixed at the declaration of the bank's insolvency." *American National Bank v. FDIC*, 710 F.2d 1528, 1540 (11th Cir. 1983). *See also* 7 Michie on Banks and Banking, Ch. 15, §§ 236, 247 (perm. ed. 1980 and supp. 1985). It is of equal certainty that the holder of a cashier's check is not entitled to preference over general creditors when the issuing bank fails before payment of the check. 10 Am. Jur. 2d *Banks* § 799 (Supp. 1983). Hence, when the cashier's checks were presented by the collecting bank, they represented an indebtedness subject to ratable dividends to be paid by the FDIC from the remaining Penn Square assets. 12 U.S.C. § 194.

Notwithstanding, it must also be kept in mind that the FDIC functioned as both receiver and insurer in this liquidating process. For this reason, the provisions of the Federal Deposit Insurance Act and the National Bank Act work, and must be read, conjunctively. Therefore, in its capacity as insurer, FDIC was required to pay each of the debts represented by the cashier's checks as insured deposits in accordance with § 1813(1)(4) and 12 C.F.R. § 330.11. Payment of any sums in excess of the insured amounts, however, would be contrary to the statutory provisions for liquidation and would create a preference of the defendants over the other creditors of Penn Square. Although defendants have argued that this is an inequitable result, it is nonetheless the harsh reality and consequence of Penn Square's insolvency.

The judgment of the trial court is reversed and the case remanded for entry of judgments in favor of plaintiffs for the difference between the amounts mistakenly paid and the insured amount to which each defendant is entitled.

[APPENDIX]

[Filed September 4, 1984]

IN THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA

FEDERAL DEPOSIT INSURANCE CORPORATION and DEPOSIT INSURANCE NATIONAL BANK OF OKLAHOMA CITY, OKLAHOMA,	)	
Plaintiffs,	)	No. CIV-83-185-W
v.	)	
PAULINE McKNIGHT,	)	
Defendant.	)	

FEDERAL DEPOSIT INSURANCE CORPORATION and DEPOSIT INSURANCE NATIONAL BANK OF OKLAHOMA CITY, OKLAHOMA,	)	
Plaintiffs,	)	No. CIV-83-186-W
v.	)	
PAULINE OIL AND GAS COMPANY,	)	
Defendant.	)	

FEDERAL DEPOSIT INSURANCE CORPORATION and DEPOSIT INSURANCE NATIONAL BANK OF OKLAHOMA CITY, OKLAHOMA,	)	
Plaintiffs,	)	No. CIV-83-188-W
v.	)	
ROCKET OIL COMPANY,	)	
Defendant.	)	

FEDERAL DEPOSIT INSURANCE CORPORATION and DEPOSIT INSURANCE NATIONAL BANK OF OKLAHOMA CITY OKLAHOMA,	)	No. CIV-83-1794-W
Plaintiffs,	)	
v.	)	
ALL SOULS EPISCOPAL CHURCH,	)	
Defendant.	)	

Sidney G. Dunagan, GABLE & GOTWALS, 20th Floor, Fourth National Building, Tulsa, Oklahoma 74119, for the plaintiffs.

Michael Paul Kirschner, John R. Denneny, George W. Dahnke and Merrilyn L. Blackburn, HASTIE AND KIRSCHNER, 3000 First Oklahoma Tower, 210 West Park Avenue, Oklahoma City, Oklahoma 73102, for the defendants Pauline McKnight, Pauline Oil and Gas Company and All Souls Episcopal Church; B. J. Rothbaum, Jr. and Ricki S. Darby, LINN & HELMS, 400 Fidelity Plaza, Oklahoma City, Oklahoma 73102, for the defendant Rocket Oil Company.

MEMORANDUM OPINION AND ORDER

Before the Honorable Lee R. West, United States District Judge

These four cases are virtually identical. The Federal Deposit Insurance Corporation ["FDIC"], in its corporate capacity as insurer of deposits in the nation's banks, and the Deposit Insurance National Bank of Oklahoma City ["DINB"], the new bank through which it paid the insured deposits of Penn Square Bank, N.A., are suing in equity for restitution of money they mistakenly paid the defendants on cashier's checks issued by Penn Square Bank prior to

its failure. Although to some degree each arises out of different facts, those facts are very similar, and the law relative to each is the same. Accordingly, they are considered here together. Fed. R. Civ. P. 42(a).

Before the Court now are cross-motions for summary judgment under Federal Rule 56. Fed. R. Civ. P. 56(a), (b). The motions are properly supported by affidavits and other evidence as required by Rule 56(e) and have been thoroughly briefed. For the reasons set forth below, the defendants' respective motions are granted, and those of the FDIC and DINB are denied.

I
A

At the threshold lies the question of the applicable substantive law. As this Court has noted in a number of earlier cases involving the FDIC arising out of the failure of Penn Square Bank, this inquiry is problematical. For example, in *Philadelphia Gear Corp. v. FDIC*, the Court reasoned:

> The applicable substantive law is derived from several sources, depending on the particular claim or defense at issue. Of course, to the extent that a claim or defense arises under the Constitution, laws, or treaties of the United States, federal law governs. *E.g., Deitrick v. Greaney*, 309 U.S. 190, 200-201 (1940); 28 U.S.C. § 1652. And in cases to which the FDIC is a party, federal common law applies if the statute itself does not provide the rule of decision. *D'Oench, Duhme & Co. v. Federal Deposit Insurance Corp.*, 315 U.S. 447, 456-59 (1941) (per Douglas, J.), 465-75 (Jackson, J., concurring). *See generally* P. Bator, P. Mishkin, D. Shapiro & H. Wechsler, *Hart and Wechsler's The Federal Courts and the Federal System* 762-70 (2d ed. 1973). However, an important source of federal common law, especially in a commercial context, is the state law under which the disputed legal relationships

arose. *See D'Oench, Duhme, supra*, 315 U.S. at 474 (Jackson, J., concurring); *Federal Deposit Insurance Corp.* v. *Bank of America National Trust & Savings Association*, 701 F.2d 831, 834-35 (9th Cir. 1983). *Accord United States* v. *Kimbell Foods*, 440 U.S. 715, 726-27, 729 (1979) (state law, incorporated as part of federal common law, determines the priority of federal Small Business Administration lien).

Philadelphia Gear, supra, No. CIV-82-1191-W (W.D. Okla. Feb. 9, 1984) (Findings of Fact and Conclusions of Law 6-7). Here, there is no federal statute governing the FDIC's restitutionary rights, so well-established federal principles of equity apply. With regard to the defendants' defenses, the Uniform Commercial Code ["UCC" or "Code"] gives content to the federal common law. *See* Section III D. *infra*. Because the Code has been enacted throughout the nation and should be interpreted in a manner that ensures uniformity, Section 1-102(2)(c), 1 U.L.A. 11 (1977), there are not any conflicts of law problems.

B

Federal Rule 56 provides that summary judgment shall be granted if "there is no genuine issue as to any material fact and . . . the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c). Summary judgment plays an important role in the Federal Rules; by avoiding the trial of cases in which there is no genuine issue of material fact, it promotes a speedy and inexpensive determination of the merits. Fed. R. Civ. P. 1. *See Washington Post Co.* v. *Keogh*, 365 F.2d 965, 968 (D.C. Cir. 1966) (per S. Wright, C.J.). However, the standard for granting summary judgment is strict. *Poller* v. *Columbia Broadcasting System, Inc.*, 368 U.S. 464, 467 (1961) (citing *Sartor* v. *Arkansas Natural Gas Corp.*, 321 U.S. 620, 627 (1944)). A motion for summary judgment must be denied unless the movant demonstrates its entitlement to it "beyond a reasonable doubt". *Bankers Trust Co.* v. *Transamerica Title*

Insurance Co., 594 F.2d 231, 235 (10th Cir. 1979) (citations omitted). On such a motion, the court must construe the facts in the light most favorable to the nonmoving party and must give that party the benefit of all reasonable inferences to be drawn from the evidence. *Adickes* v. *S. H. Kress & Co.*, 398 U.S. 144, 153-59 (1970).

II

The facts are not in dispute. On July 2, 1982, certain certificates of deposit ["CD's"] issued by Penn Square Bank to Pauline Oil and Gas matured, and Mrs. McKnight elected to withdraw the proceeds of those CD's. Thus, Penn Square Bank issued its cashier's check no. 195662 to Pauline Oil and Gas in the amount of $140,226.41. At that same time, Mrs. McKnight decided to cash another CD issued by the Bank jointly to her and her mother Mrs. Burkhart, even though this latter CD had not matured. In exchange for the proceeds of this CD, the Bank issued Mrs. McKnight its cashier's check no. 195663 in the amount of $183,312.05.

Similarly, Rocket Oil owned Penn Square Bank CD 19169 in the amount of $1.5 million. On July 1, 1982, Rocket redeemed its CD, which at that time was worth $1,480,273.98, and those funds were used to purchase Penn Square Bank cashier's check 195657 in a like amount. Subsequently, Rocket Oil deposited this check in the Oklahoma National Bank of Duncan.

Finally, on July 2, 1982, All Souls Episcopal Church exchanged two CD's issued by Penn Square Bank and commercial paper issued by First Penn Corporation, the Bank's parent holding company, for three Penn Square Bank cashier's checks. Those checks totaled $452,527.25: no. 195660 in the amount of $176,307.31; no. 195661 in the amount of $166,224.99; and no. 195690 in the amount of $109,994.95. Later on July 2, All Souls deposited these three cashier's checks with Fidelity Bank, N.A., of Oklahoma City ["Fidelity"], and in exchange Fidelity issued to All Souls a CD for the total amount of the checks.

Significantly, there is absolutely no evidence that any of these parties knew of Penn Square Bank's impending failure.

At about 7:00 p.m. on Monday, July 5, 1982, the Comptroller of the Currency of the United States declared Penn Square Bank insolvent under 12 U.S.C. § 191 and appointed the FDIC to act as its receiver under 12 U.S.C. § 1821(c). The FDIC in its corporate capacity then organized DINB as a new bank through which to make available to depositors the insured portions of their deposits. *See* 12 U.S.C. § 1821(f), (h). Thereupon, the FDIC transferred to DINB an amount equal to Penn Square Bank's insured deposits plus DINB's estimated operating expenses. *See id.* § 1821(j). These amounts were transferred from the FDIC's Permanent Insurance Fund. *See id.* § 1821(a).

Immediately, the FDIC's employees prepared to handle checks and other items drawn against the accounts of Penn Square Bank's customers. In doing so, they compiled a list of 4,000 of the Bank's approximately 25,000 accounts and "flagged" each of those accounts in the Bank's computer so that it would reject any transaction in excess of the deposit insurance limit of $100,000. However, through oversight, no such system was installed to monitor cashier's checks drawn by the Bank on itself until Wednesday, July 7, 1982. Affidavit of Steve W. Black, FDIC Liquidation Specialist, Exhibit 1 to Plaintiffs' Motion for Summary Judgment Against Pauline McKnight and Pauline Oil and Gas Co. (Dec. 14, 1983) ["Black Affidavit"].

On Tuesday, July 6, 1982, as part of the normal collection process, Fidelity presented to DINB cashier's checks 195657, 195660, 195661, 195662, 195663, and 195690.[1] DINB

[1] As to certain of these items, Fidelity was a depositary bank, and as to others it was an intermediary bank under the Uniform Commercial Code. *See* UCC §4-105, 2A U.L.A., *supra*, at 29. These different capacities, however, are not material here.

paid these items in full by settling accounts with Fidelity through the Federal Reserve Bank.

On July 14, 1982, Fidelity filed an interpleader action to determine who was entitled to the funds it had collected, but on October 22, 1982, its action was dismissed. *Fidelity Bank, N.A.* v. *FDIC*, No. CIV-82-1042-R (W.D. Okla.). The FDIC and DINB then instituted these actions in 1983.

III

A

In general, a person who is unjustly enriched by a mistaken payment from another owes restitution to him as a matter of equity. *See Restatement of Restitution* §§ 1, 15-27, 46-54 (1937); *Restatement (Second) of Restitution* §§ 1, 5 (Tent. Draft No. 1, 1983); D. Dobbs, *Handbook of the Law of Remedies* §§ 4.1, 4.3, 11.1, 11.8 (1973). This general rule applies with equal force where an agency of the United States, rather than a private party, mistakenly pays money to another. *See, e.g., United States* v. *Wurts*, 303 U.S. 414, 415 (1938); *Woods* v. *United States*, 724 F.2d 1444, 1448 (9th Cir. 1984); *Aetna Casualty & Surety Co.* v. *United States*, 526 F.2d 1127, 1130 (Ct. Cl. 1975). Finally, the rule also applies to banks. *E.g., Bank of Naperville* v. *Catalano*, 86 Ill.App.3d 1005, 408 N.E.2d 441 (1980). *See* 5A Michie, *Banks and Banking*, ch. 9, § 230 (1983); Annot., 10 A.L.R. 4th 524 (1981).

Here, the plaintiffs have established a *prima facie* case for restitution of money mistakenly paid. When Penn Square Bank was declared insolvent on July 5, 1982, each of the defendants had an unpaid cashier's check or checks drawn by Penn Square Bank on itself. At that time, each defendant was entitled to $100,000.00 in deposit insurance, *see* Federal Deposit Insurance Act § 3, 12 U.S.C. § 1813(l)(4), (m)(1); 12 C.F.R. pt. 330 (1984), and a ratable distribution from the assets of the failed Bank on the uninsured balance, *see* 12 U.S.C. § 91, 194. Nevertheless, the FDIC in its corporate capacity, through DINB, mistakenly paid these

cashier's checks in full on July 6 because their employees failed to "flag" that account in Penn Square Bank's computer until July 7, so that it would reject any transaction in excess of the deposit insurance ceiling. Black Affidavit, *supra*.

B

However, if an action for restitution is predicated on a negotiable instrument, then special rules apply as defenses. *See Restatement of Restitution, supra*, §§ 29-38; *Restatement (Second) of Restitution, supra*, § 1 comm. n.; D. Dobbs, *supra*, § 4.7 at 287-92. Of particular importance here is the final payment rule. *See* Order 4-7 (June 23, 1983). Section 3-418 of the UCC provides, in pertinent part, that "payment or acceptance of any instrument is final in favor of a holder in due course. . ."[2] Uniform Commercial Code, § 3-418, 2 U.L.A., *supra*, at 494. The modern rationale underpinning the final payment rule is repose; as the drafters of the Code put it, "it is highly desirable to end the transaction on an instrument when it is paid rather than reopen and upset a series of commercial transactions at a later date" when a problem is detected. *Id.* official comm. 1, 2. Effectively, the rule bars an action for restitution against a holder in due course. J. White & R. Summers, *Handbook of the Law Under the Uniform Commercial Code* § 16-2 at 609-12 (2d ed. 1980); *Restatement (Second) of Restitution, supra*, § 1 comm. n. *Contra Bank Leumi Trust Co. of New York* v. *Bally's Park Place, Inc.*, 528 F.Supp. 349, 354 (S.D.N.Y. 1981).

Here, the defendants have satisfied the final payment rule, so the plaintiffs' actions are barred. First, the dis-

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[2] The remaining provisions of Section 3-418 are not relevant here. First, the plaintiffs do not argue that they may recover under Section 4-301 or that the defendants are liable under Section3-417 for breach of warranty on presentment. Second, the defendants do not contend that they changed their positions in good faith reliance on payment. *See* UCC §3-418, 2 U.L.A., *supra*, at 494

puted cashier's checks are "instruments" within Section 3-418 of the Code. *See TPO Inc.* v. *FDIC*, 487 F.2d 131, 136 (3d Cir. 1973); UCC § 3-118(a), 2 U.L.A., *supra*, at 99. *But see Santos* v. *First National State Bank of New Jersey*, 186 N.J. Super. 52, 451 A.2d 401, 407-408 (N.J. Super. Ct. App. Div. 1982). Second, when DINB settled with Fidelity through the Federal Reserve Bank, the cashier's checks were finally paid. UCC § 3-418, 2 U.L.A., *supra*, at 494; § 4-213(1), 2A U.L.A., *supra*, at 107. *See* J. White & R. Summers, *supra*, §§ 16-2 at 611 & 16-4; 3 R. Anderson, *Uniform Commercial Code* §§ 4-213:1, 4-213:4 (1972 & Supp. 1983); Annot., 23 A.L.R. 4th 203 (1983).

Third, the defendants are holders in due course. Section 3-302 of the Code defines a holder in due course as one who takes an instrument for value, in good faith, and without notice that it is overdue or has been dishonored or of any defense or claim to it on the part of any person. UCC § 3-302(1), 2 U.L.A., *supra*, at 176. Clearly, the defendants paid value for their cashier's checks; specifically, they used the proceeds of their Penn Square Bank CD's or First Penn commercial paper, which they had redeemed. Additionally, there is no evidence that the defendants acted in bad faith[3] or had notice of any defense or claim against the cashier's checks when they purchased them; indeed, at that time, there were no claims or defenses to the instruments. Finally, it is now settled that a payee may be a holder in due course. UCC § 3-302(2) & official comm. 2, 2 U.L.A., *supra*, at 17-77. *See* J. White & R. Summers, *supra*, § 14-7; 2 R. Anderson, *Uniform Commercial Code* § 3-302:19 (1971 & Supp. 1983).

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[3] Significantly, the factual issue of good faith *vel non* was the sole barrier to granting defendants' motions to dismiss in *McKnight, Pauline Oil & Gas, and Rocket Oil*. Order, *supra*, at 4-7.

C

Furthermore, in their motions for summary judgment the defendants contend that the plaintiffs' actions are barred by Section 4-213 of the Code, regardless of whether they were holders in due course or changed their positions in good faith reliance on final payment. Section 4-213 provides:

> (1) An item is finally paid by a payor bank when the bank has done any of the following, whichever happens first:
>
> (a) paid the item in cash; or
>
> (b) settled for the item without reserving a right to revoke the settlement and without having such right under statute, clearing house rule or agreement; or
>
> (c) completed the process of posting the item to the indicated account of the drawer, maker or other person to be charged therewith; or
>
> (d) made a provisional settlement for the item and failed to revoke the settlement in the time and manner permitted by statute, clearing house rule or agreement. Upon a final payment under subparagraphs (b), (c) or (d) the payor bank shall be accountable for the amount of the item.
>
> (2) If provisional settlement for an item between the presenting and payor banks is made through a clearing house or by debits or credits in an account between them, then to the extent that provisional debits or credits for the item are entered in accounts between the presenting and payor banks or between the presenting and successive prior collecting banks seriatim, they become final upon final payment of the item by the payor bank.
>
> (3) If a collecting bank receives a settlement for an item which is or becomes final (subsection (3) of Sec-

tion 4-211, subsection (2) of Section 4-213) the bank is accountable to its customer for the amount of the item and any provisional credit given for the item in an account with its customer becomes final.

(4) Subject to any right of the bank to apply the credit to an obligation of the customer, credit given by a bank for an item in an account with its customer becomes available for withdrawal as of right

(a) in any case where the bank has received a provisional settlement for the item, — when such settlement becomes final and the bank has had a reasonable time to learn that the settlement is final;

(b) in any case where the bank is both a depository bank and a payor bank and the item is finally paid, — at the opening of the bank's second banking day following receipt of the item.

(5) A deposit of money in a bank is final when made but, subject to any right of the bank to apply the deposit to an obligation of the customer, the deposit becomes available for withdrawal as of right at the opening of the bank's next day following receipt of the deposit.

UCC §4-213, 2A U.L.A., *supra*. at 107-108.

Final payment of an item is important for a number of reasons. It is one of several factors determining the relative priorities between items and notices, stop-orders, legal process and set-offs (Section 4-303). It is the "end of the line" in the collection process and the "turn around" point commencing the return flow of proceeds. It is the point at which many provisional settlements become final. See Section 4-213(2). Final payment of an item by the payor bank fixes preferential rights under Section 4-214(1) and (2).

Id. official comm. 1.

There is a paucity of relevant case law interpreting Section 4-213. On the one hand, two courts have indicated that Section 4-213 protects those who are not holders in due course, although the Courts did not so hold. *Ashford Bank* v. *Capital Preservation Fund, Inc.*, 544 F.Supp. 26, 28-29 (D. Mont. 1982); *Kirby* v. *First and Merchants National Bank*, 210 Va. 88, 168 S.E.2d 273, 275 n. 4 (1969). Further, Professors White and Summers have argued in favor of this interpretation in the second edition of their authoritative treatise. J. White & R. Summers, *supra*, §16-2 at 613-18. On the other hand, however, the better reasoned cases which have addressed the issue squarely have held that Section 4-213 does not bar an action for restitution against one who neither is a holder in due course nor has detrimentally relied on final payment. *National Savings and Trust Co.* v. *Park Corp.*, 722 F.2d 1303, 1305-1306 (6th Cir. 1983), *cert. denied*, 104 S.Ct. 1916 (1984); *Demos* v. *Lyons*, 151 N.J. Super. 489, 376 A.2d 1352, 1355-57 (N.J. Super. Ct. Law Div. 1977). These latter cases are far more persuasive, and the Court adopts them here as authoritative.

D

Finally, the FDIC argues in response that once a national bank is declared insolvent and closed, the final payment rule is ineffective *ipso facto* as a defense to an action for restitution of money paid by mistake. This argument may apply in certain instances, but it is not tenable here. For example, if money is mistakenly paid out of the assets of a failed national bank such that the payee is preferred over other uninsured depositors and general creditors, then that payment is "utterly null and void" under the National Bank Act, 12 U.S.C. §91, and a defense based on state law or even federal common law cannot negate that which the statute commands. *See* U.S. Const. art. VI. In the cases at bar, however, the mistaken payment was made out of assets transferred from the FDIC's Permanent Insurance Fund to DINB. There are no federal statutes or even judicial decisions which preclude the assertion of the final payment

rule in such a circumstance; quite the contrary, the FDIC as an agency of the United States is to be treated as any other party. *Cf., e.g., Clearfield Trust Co.* v. *United States*, 318 U.S. 363, 369 (1943) ("The United States as drawee of commercial paper stands in no different light than any other drawee.").

When the FDIC organized DINB to make available the insured deposits in Penn Square Bank after the Bank had failed, they assumed a host of attendant duties. In particular, they stepped into the complex and arcane world of bank collections, for when the Bank failed, there were surely myriad items being processed. As the authors of the Code noted:

> It must be remembered that in bank collections as a whole and in the handling of items by an individual bank, items go through a whole series of processes. It must also be remembered that at any particular point of time a particular bank (at least one of any size) is functioning as a depositary bank for some items, as an intermediary bank for others, as a presenting bank for still others and as a payor bank for still others, and that when it suspends payments it will have close to its normal load of items working through its various processes.

UCC §4-214 official comm. 1, 2A U.L.A., *supra*, at 119-20.

Therefore, the salient issue is at what point in those processes has an item progressed far enough that it should be completed, instead of being sent back and reversing all the steps in those processes. That point is final payment as defined in Section 4-213(1). *See id.*[4] At that point, the

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[4] Section 4-214 of the Code does not itself apply to national banks, *id.* official comm. 3, because federal law forbids preferential treatment in distributing the assets of an insolvent national bank, 12 U.S.C. §91. Nonetheless, the drafters' comments to Section 4-214 are an invaluable guide in determining the policies which should inform the Court's decision. *See, e.g.*, National Savings & Trust Co. v. Park Corp., *supra*, 722 F.2d at 1306.

bank becomes accountable for the item under Section 4-213(1), and an action for restitution is barred by Section 3-418. Here, the cashier's checks in dispute were finally paid, and the FDIC may not obtain restitution of the money it paid in excess of the deposit insurance limit. The rationale of repose requires that it bear the loss.[5]

IV

Accordingly, the plaintiffs' motions for summary judgment are denied, and the defendants' motions for summary judgment are granted.

IT IS SO ORDERED this 4th day of September, 1984.

(s) *Lee R. West*
LEE R. WEST
United States District Judge

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[5] Actually, that loss is not total. It appears that the FDIC in its corporate capacity is thereby subrogated to the payees' rights in the assets of the failed bank, 12 U.S.C. §821(g), giving it the right to share ratably in the estate, 12 U.S.C. §194.